ALJ/TIM/hl2 **DRAFT** Agenda ID #5677
Ratesetting

Decision **PROPOSED DECISION OF ALJ KENNEY** (Mailed 5/16/2006)

BEFORE THE PUBLIC UTILITIES COMMISSION OF THE STATE OF CALIFORNIA

Order Instituting Investigation on the Commission's Own Motion into the Rates, Operations, Practices, Service, and Facilities of Pacific Gas and Electric Company (U 39-M).	Investigation 06-03-003 (Filed March 2, 2006)
Application of Pacific Gas and Electric Company (U 39-M) to Increase Gas and Electric Revenue Requirements, Rates, and Charges for a Pension Contribution, Effective January 1, 2006.	Application 05-12-021 (Filed December 20, 2005)
Application of Pacific Gas and Electric Company (U 39-M) for Authorization, Among Other Things, to Increase Rates and Charges for Electric and Gas Service Effective on January 1, 2007.	Application 05-12-002 (Filed December 2, 2005)

OPINION AUTHORIZING PACIFIC GAS AND ELECTRIC COMPANY TO RECOVER CONTRIBUTIONS TO ITS EMPLOYEE PENSION PLAN

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1. Summary

This Decision adopts an uncontested settlement agreement (Settlement) that authorizes Pacific Gas and Electric Company's (PG&E) to recover contributions to its employee pension plan (Pension Plan) during 2006 – 2009. The purpose of the contributions is to restore the funded status of the Pension Plan to 100% by January 1, 2010. The parties to the Settlement are PG&E, the Division of Ratepayer Advocates (DRA), and the Coalition of California Utility Employees (CCUE). The Settlement resolves the pension issues in Application (A.) 05-12-002 and all issues in A.05-12-021.

The Settlement requires PG&E to contribute $249.7 million to its Pension trust in 2006 and $153.4 million annually in 2007 - 2009. The associated revenue requirement is divided among PG&E's lines of business. This Decision is being issued in PG&E's general rate case (GRC) proceeding and authorizes PG&E to recover the following revenue requirement for its GRC lines of business:

$ Millions				
GRC Line of Business	**2006**	**2007**	**2008**	**2009**
Electric Distribution	77.2	46.8	48.4	50.5
Gas Distribution	34.5	26.2	27.2	28.3
Electric Generation	43.3	25.3	26.2	27.3
GRC Total	155.0	98.2	101.7	106.1

The pension contributions are fixed by the Settlement Agreement, while the revenue requirement shown in the above Table for 2007 – 2009 is based on numerous assumptions (e.g., capitalization factors and deprecation rates) that are subject to litigation in this proceeding and others. Consequently, the actual revenue requirement for 2007 - 2009 may change.

The adopted Settlement requires PG&E to establish a two-way balancing account to track the difference between authorized contributions to PG&E's Pension trust and (1) lower contributions for any reason, or (2) federally mandated higher contributions. PG&E will file an annual report stating the amount of pension contributions and the dates the contributions were made.

Finally, this Decision declines to adopt the proposal by The Utility Reform Network (TURN) to allow PG&E to place up to 50% of its Pension trust's equity investments in securities issued by the utility companies that PG&E used to support its requested return on equity (ROE) of 11.50% in A.05-05-006. TURN's proposal is not adopted because TURN has not shown that its proposal would enhance the risk-adjusted return for PG&E's Pension trust assets.

Application 05-12-021 is closed. Application 05-12-002 and the companion Investigation 06-03-003 remain open to address the remaining issues in PG&E's GRC proceeding.

2. Background

PG&E provides pension benefits to most of its employees. Pension benefits are funded through a tax-qualified trust that is subject to the Employee Retirement Income Security Act of 1974 (ERISA). PG&E did not make, or recover in rates, any contributions to its Pension trust during 1992 - 2005.[1] This was made possible by high returns on Pension trust assets during the 1990s.

On December 2, 2005, PG&E filed GRC A.05-12-002 in which PG&E requests, among other things, authority to (1) contribute $343.9 million annually

[1] PG&E shareholders continued to fund contributions to Voluntary Retirement Incentive (VRI) programs during this period.

to its Pension trust during 2007-09, and (2) recover an associated revenue requirement of $216.2 million annually in 2007-09 for the GRC lines of business.[2]

In Decision (D.) 05-12-046, the Commission authorized PG&E to (1) make a contribution to its Pension trust ("pension contribution") for calendar year 2006; (2) recover the pension contribution in rates effective January 1, 2006, subject to refund; and (3) file an application for authority to recover the pension contribution. In response to D.05-12-046, PG&E filed A.05-12-021 for authority to make a pension contribution of $249.7 million in 2006, with an associated revenue requirement for PG&E's GRC lines of business of $155.0 million in 2006. Approving A.05-12-021 would reduce the pension contributions and revenue requirement that PG&E requested in A.05-12-002 for 2007-09.

Pursuant to D.05-12-046, PG&E filed Advice Letter (AL) 2686-G/2753-E on December 20, 2005, to collect in rates beginning on January 1, 2006, a pension contribution revenue requirement for 2006 of $155.0 million. The AL also established a mechanism to refund the $155 million to the extent the Commission denied PG&E's request in A.05-12-021 to recover the $155 million. AL 2686-G/2753-E went into effect automatically.

A joint pre-hearing conference for A.05-12-002 and A.05-12-021 was held on January 23, 2006. On March 8, 2006, PG&E, DRA, and CCUE filed a Settlement Agreement that resolves all issues in A.05-12-021 and the pension contribution issues in A.05-12-002. The Commission held an evidentiary hearing regarding the Settlement on March 20, 2006. On March 21, 2006, the assigned

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[2] The actual revenue requirement would be higher in 2008-09 due to attrition adjustments.

Administrative Law Judge (ALJ) issued a ruling that consolidated A.05-12-002 and A.05-12-021 for the limited purpose of considering the Settlement.

There was no opposition to the Settlement Agreement. Opening briefs regarding the Settlement were filed on March 27, 2006, by TURN and jointly by PG&E, DRA, and CCUE (the Settling Parties). The Settling Parties filed a reply brief on April 4, 2006. There were no requests for a final oral argument. In response to inquiries from the assigned ALJ, PG&E provided supplemental information regarding the Settlement via email to the service list.

3. Applications 05-12-002 and 05-12-021

The funded status of PG&E's Pension Plan on January 1, 2005, was 98.6%. (i.e., trust assets were 98.6% of pension liabilities). PG&E projects that if no pension contributions are made during 2006-08, the funded status will decline to 90.3% by January 1, 2009, and PG&E will be required by ERISA to make a pension contribution of $308.0 million in 2009. To project the Pension Plan's funded status, PG&E assumed its Pension trust assets will earn an annual return of 7.0%. The Pension trust fund is invested 60% in stocks and 40% in bonds. The fair value of the trust fund assets was $8.049 billion on December 31, 2005.[3]

In A.05-12-002 and A.05-12-021, PG&E requests authority to restore the Pension Plan's funded status to 100% by January 1, 2010, by contributing $249.7 million annually to the Pension trust fund during 2006-09.[4] These

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[3] PG&E Form 10-K for 2005, Note 14 to the Financial Statements. We take official notice of PG&E's Form 10-K pursuant to Rule 73 of the Commission's Rules of Practice and Procedure (Rule).

[4] By comparison, PG&E's total pension expense in 2005 under Generally Accepted Accounting Principles (excluding VRI and PG&E Corporation) as reported in its Form 10-K was $173 million. (Settling Parties' opening brief, p. 9.)

contributions will cover the cost of the benefits earned annually, plus amortize the unfunded liability.

PG&E contends that it would be imprudent to limit contributions to the minimum required by ERISA. PG&E states that ERISA allows pension plan sponsors to accrue a credit balance when they contribute more than the minimum required amount, and then draw down the credit balance in later years. The problem with the credit-balance rules, according to PG&E, is that the rules ignore the funded status of the plan.

PG&E's Pension Plan has a credit balance, which allows PG&E to defer contributions until 2009. At that time, pension liabilities will exceed assets by $874 million. The minimum contribution required by ERISA will be $308 million in 2009, $735 million in 2010, and $635 million in 2011. PG&E argues that using the credit balance to defer contributions to an underfunded pension plan is equivalent to charging current expenses to a credit card while deferring all payments to the future. The outcome would be a growing unfunded pension liability that reduces benefit security and shifts contribution requirements to future ratepayers when the credit balance is exhausted.

For ratemaking purposes, PG&E intends to allocate the annual pension contributions between expense and capital. The annual revenue requirement would be the sum of (1) the expensed portion of the pension contribution, (2) the depreciation, rate-of-return, and taxes on the capitalized portion, and (3) franchise fees and uncollectibles (FF&U). The following Table shows the annual contributions for 2006-09 and the associated revenue requirement:

($MILLIONS)

	2006	2007	2008	2009
Total Cash Contribution	273.2	273.2	273.2	273.2
PG&E Corp. Contribution	(3.2)	(3.2)	(3.2)	(3.2)
Voluntary Retiremt. Incentives (VRI)	(20.2)	(20.2)	(20.2)	(20.2)
Net Contribution	249.7	249.7	249.7	249.7
Revenue Requirement	176.5	178.8	185.2	193.2
Source: Attachment 2 of PG&E Email sent on April 21, 2006.				

The pension contributions for PG&E Corp. and VRI are excluded from rates. The above Table shows that even though the pension contributions remain level during 2006-09, the revenue requirement steadily increases. This is due to the accumulation of capitalized pension contributions, which results in rising costs for deprecation, rate-of-return, etc. The revenue requirement shown in the above Table (and throughout today's Decision) is based on a myriad of factors that are subject to change in this proceeding and others (e.g., depreciation rates, rate-of-return, FF&U, etc.). Thus, the revenue requirement shown in the above Table is an estimate.

PG&E intends to allocate its pension revenue requirement among its lines of business as follows:

Allocation of Requested Revenue Requirement ($Millions)				
	2006	**2007**	**2008**	**2009**
Electric Distribution	77.2	75.1	77.8	81.2
Gas Distribution	34.5	42.1	43.6	45.5
Electric Generation	43.3	40.6	42.0	43.9
GRC Subtotal	***155.0***	***157.8***	***163.4***	***170.6***
Nuclear Decommissioning	0.8	0.9	0.9	1.0
Electric Transmission	11.6	11.6	12.1	12.6
Gas Transmission & Storage	9.1	8.5	8.8	9.1
Non-GRC Subtotal	***21.5***	***21.0***	***21.8***	***22.7***
Total Company	**176.5**	**178.8**	**185.2**	**193.3**
Source: PG&E Email Sent on April 21, 2006, Attachment 2				

The GRC revenue requirement shown in the above Table includes electric and gas public purpose programs.

PG&E requests that the pension revenue requirement for nuclear decommissioning be determined in the instant proceeding, and then recovered in PG&E's Nuclear Decommissioning Cost Triennial Proceeding (A.05-11-009). PG&E does not request recovery of pension costs for electric transmission from the Commission, since costs for electric transmission are under the jurisdiction of the Federal Energy Regulatory Commission (FERC). Nor does PG&E request recovery of pension costs for the gas transmission and storage (GT&S) in the instant proceeding. PG&E explains that costs for GT&S are governed by a settlement agreement adopted in D.04-12-050 that will remain in effect through 2007. Hence, PG&E cannot recover pension costs allocable to GT&S until 2008.

PG&E proposes that the Commission adopt a two-way (symmetrical) balancing account for pension costs, beginning in 2007. The balancing account would track the difference between actual and adopted costs.

4. The Settlement Agreement

On March 10, 2006, PG&E filed a Settlement Agreement pursuant to Rule 51 *et seq.*, on behalf of itself, DRA, and CCUE. The Settlement authorizes PG&E to recover pension contributions in 2006-09 that will result in PG&E's Pension Plan being fully funded on January 1, 2010, on a projected basis. The Settlement resolves all issues in A.05-12-021 and the pension issues in A.05-12-002. A copy of the Settlement Agreement is attached to today's Decision.

The Settlement differs in three respects from PG&E's requests in A.05-12-002 and A.05-12-021. First, the Settlement takes into account the 2005 year-end return on Pension trust assets (information that was not available when PG&E filed A.05-12-021). Second, the Settlement makes final (i.e., not subject to refund) the $155 million that PG&E is currently collecting in rates in 2006 pursuant to D.05-12-046. Finally, the Settlement assumes that PG&E's Pension trust assets will earn 7.5% annually, versus 7.0% used by PG&E in A.05-12-002 and A.05-12-021. These three adjustments reduce PG&E's pension contributions and associated revenue requirement in 2007-2009. There is no change to PG&E's requested pension contribution and revenue requirement for 2006. The following Table compares PG&E's request in A.05-12-002 and A.05-12-021 with the Settlement Agreement:

(Millions)

	Requested by PG&E (2006 / annually 2007-09)	**Settlement** (2006/annually 2007-09)
Total Contribution	$273.2 / $273.2	$273.2 / $176.0
Net Contribution, excl. VRI & PG&E Corp.	$249.7 / $249.7	$249.7 / $153.4
Total Company Revenue Requirement*	$176.5 / $178.8	$176.5 / $111.3
GRC Revenue Requirement	$155.0 / $157.8	$155.0 / $98.2
* The amounts for 2007—09 reflect many assumptions that are subject to change.		

The Settlement does not alter PG&E's proposed treatment of pension costs for nuclear decommissioning, electric transmission, and gas transmission described previously.

The Settlement authorizes PG&E to establish a two-way balancing account for 2007-09 for differences between authorized pension contributions and (1) lower contributions for any reason, or (2) federally mandated higher contributions. The account balance, if any, would (i) accrue interest at the 3-month commercial paper rate, as reported in the Federal Reserve Statistical Release, and (ii) be amortized annually in conjunction with the Annual Electric True-Up (AET) and Annual Gas True-Up (AGT) processes via the Distribution Revenue Adjustment Mechanism (DRAM), Utility Generation Balancing Account (UGBA), Core Fixed Cost Account, and Non-core Distribution Fixed Cost Account.[5] PG&E would file an advice letter to establish the balancing account within 60 days from today's Decision.[6]

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[5] First PG&E email sent on April 28, 2006.

[6] Second PG&E email sent on April 28, 2006.

The Settlement Agreement retains PG&E's proposal in A.05-12-002 and A.05-12-021 to file an annual report that shows PG&E's actual pension contributions for the prior year and the dates the contributions were made. PG&E would file the report no later than February 15th of 2007 through 2010.[7]

5. TURN's Response to the Settlement

The only response to the Settlement Agreement came from TURN in the form of a brief filed after the evidentiary hearing on the Settlement. TURN is neutral on the Settlement, but is concerned about the disparity between the projected earnings on PG&E's Pension trust fund equity investments of 8.0% and PG&E's authorized ROE of 11.35%.[8]

TURN notes that PG&E's Pension trust fund currently has 60% of its assets invested in equity securities. TURN proposes that the Commission allow PG&E to place up to 50% of the trust fund's equity investments in the companies that PG&E used to support its ROE request in the most recent cost of capital proceeding, A.05-05-006. There, PG&E requested an ROE of 11.50% for 2006 based, in large part, on 36 comparable utility companies that PG&E used as its proxy group in its financial models. TURN argues that PG&E's position in A.05-05-006 demonstrates that PG&E expects the companies it identified as its proxy group will earn significantly more than PG&E's Pension trust fund. TURN states that its proposal would allow PG&E's Pension trust fund to invest in higher yielding assets, which should reduce pension costs over time.

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[7] First PG&E email sent on April 28, 2006.

[8] D.05-12-043 authorized an ROE for PG&E of 11.35%

6. The Settling Parties' Reply to TURN

The Settling Parties contend that TURN's proposal does not comply with ERISA, which requires that fiduciaries discharge their duties "with the care, skill, prudence, and diligence…that a prudent man acting in a like capacity and familiar with such matters would use…" (ERISA, Section 404(a)(1)(B).) They state that TURN's proposal would allow PG&E to place 50% of the Pension trust's equity investments in a single industry that represents just 3.5% of the U.S. stock market (i.e., the 36 utility companies PG&E used as its proxy group in its financial models). The Settling Parties assert that weighting the Pension trust fund's utility industry exposure at 50% – over 14 times the 3.5% weighting of the utility industry in the U.S. stock market – would be inconsistent with principle of diversification and, therefore, violate the ERISA standard of care.

7. Discussion

We have a strong public policy favoring the settlement of disputes. This policy supports many worthwhile goals, including reducing the expense of litigation, conserving Commission resources, and allowing parties to reduce the risk that litigation will produce unacceptable results. Our policy weighs against the Commission's alteration of agreements reached through negotiation. As long as a settlement taken as a whole is reasonable in light of the record, consistent with the law, and in the public interest, it should be adopted without alteration.

The Settling Parties state that the Settlement is an all-party agreement. In such cases, the Commission applies two complementary sets of criteria set forth in Rule 51.1(e) and D.92-12-019. For the reasons set forth below, we find that the Settlement Agreement satisfies these criteria, and we will adopt it.

A. Rule 51.1(e) Criteria

Rule 51.1(e) requires that a settlement be reasonable in light of the whole record, consistent with the law, and in the public interest.

The first Rule 51.1(e) criterion is that the Settlement must be reasonable in light of the whole record. The record for this proceeding includes the oral and written testimony that was received into evidence at the hearing on March 20, 2006; the parties' briefs; and supplemental information that PG&E emailed to the service list in response to inquires from the assigned ALJ. After reviewing the whole record, we conclude that the Settlement is reasonable because (1) there is no opposition to the Settlement; (2) the central purpose of the Settlement is reasonable, i.e., to allow PG&E to recover pension contributions necessary for its Pension Plan to reach a funded status of 100% by 2010; (3) the calculation of the contributions was determined by well qualified experts; and (4) PG&E must use the pension contributions collected in rates for their intended purpose or refund the contributions to ratepayers, with interest.

The next Rule 51.1(e) criterion is whether the Settlement is consistent with the law. There is no indication in the record of this proceeding that the Settlement is contrary to any laws or prior Commission decisions. Therefore, we find that the Settlement satisfies this criterion.

The final Rule 51.1(e) criterion is whether the Settlement is in the public interest. The provision of pension benefits to utility employees is a necessary part of the overall cost of providing gas and electric service to the public. We conclude that the Settlement is in the public interest because it allows PG&E to recover a reasonable amount of pension costs.

B. D.92-12-019 Criteria

Decision 92-12-019 established the following requirements for all-party settlements:

a. The settlement is sponsored by all active parties;
b. The sponsoring parties are fairly reflective of the affected interests;
c. No term of the settlement contravenes statutory provisions or prior Commission decisions; and
d. The settlement conveys sufficient information to permit the Commission to discharge its future regulatory obligations with respect to the parties and their interests.[9]

We find that the Settlement meets criterion "a." because the Settling Parties are all the active parties on pension issues (i.e., those parties that chose to participate actively in the settlement conference on February 24, 2006, and in the evidentiary hearing on March 20, 2006).[10] The Settlement meets criterion "b." because DRA, CCUE, and PG&E are fairly representative of the interests of PG&E's customers, employees, and shareholders, respectively. The Settlement meets criterion "c." because it is consistent with law, as explained previously. Finally, the Settlement meets criterion "d." because the Settlement and the supporting record contain sufficient information to implement the Settlement.

For the preceding reasons, we find that the Settlement Agreement satisfies Rule 51.1(e) and D.92-12-019. Therefore, we will adopt the Settlement. In

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[9] D.92-12-019, 46 CPUC 2d 538, 550-551.

[10] In its brief regarding the Settlement, TURN states that it is "neutral on the settlement itself" (TURN Brief, page 1.), and devotes the remainder of its brief to matters not directly related to the Settlement. Under these circumstances, we conclude that the Settlement was submitted by all the active parties.

accordance with Rule 51.8, the adopted Settlement is binding on all parties to A.05-12-002 and A.05-12-021. With one exception, our adoption of the Settlement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding or in any future proceeding. The one exception is that the pension-related revenue requirement established in other proceedings should be consistent with the Settlement Agreement.

C. Implementation of the Settlement Agreement

PG&E shall make contributions to its Pension trust and recover the contributions in rates as set forth in the Settlement Agreement. The Settlement requires PG&E to contribute $273.2 million for calendar year 2006, which equates to a net contribution (excluding VRI and PG&E Corp.) of $249.7 million. PG&E must make the contribution no later than 40 days from the effective date of today's Decision. PG&E is already collecting $155 million in rates pursuant to D.05-12-046 for the associated GRC revenue requirement.

For 2007, 2008, and 2009, the Settlement requires PG&E to annually contribute $176.0 million, which equates to a net contribution of $153.4 million. PG&E must make quarterly contributions on April 15, July 15, October 15 and January 15 for each annual payment cycle. The GRC-related revenue requirement is $98.2 million in 2007, $101.7 million in 2008, and $106.1 million in

2009.[11] The annual revenue requirement will be implemented via the AET and AGT processes.[12]

PG&E may recover the pension revenue requirement for nuclear decommissioning in A.05-11-009, the Nuclear Decommissioning Triennial Cost Proceeding. For gas transmission, PG&E may not request any pension revenue requirement until 2008 pursuant to D.04-12-050. For electric transmission, PG&E may seek to recover the pension revenue requirement from FERC.

Consistent with the Settlement Agreement, PG&E shall file an advice letter to establish a two-way balancing account for differences between authorized contributions to the Pension trust and (1) lower contributions for any reason, or (2) federally mandated higher contributions. The differences between PG&E's authorized revenue requirement for pension contributions and the amount collected in rates will be tracked and trued-up by the various balancing accounts that implement PG&E's GRC revenue requirement, (i.e., DRAM, UGBA, etc.). PG&E shall file the advice letter no later than 60 days from the effective date of today's Decision. As long as the advice letter conforms to today's Decision, the Energy Division may approve the advice letter without a Commission resolution.

Finally, as provided for in the Settlement Agreement, PG&E shall file an annual report with the Commission, with service to DRA and CCUE, verifying the amount of pension contributions and dates the contributions were made.

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[11] The Settlement Agreement shows that the GRC revenue requirement is $98.2 million annually during 2007-09. This amount does not reflect the steadily increasing revenue requirement from the accumulation of capitalized pension costs. (PG&E email sent on April 21, 2006.)

[12] As mentioned previously, the actual revenue requirement for 2007-2009 will be based on numerous factors that are subject to change.

The report shall also include the value of pension assets at year end. PG&E shall file the report no later than February 15th during 2007-2010.

D. The Pension Interest Memorandum Account

Pursuant to D.05-12-046, PG&E filed three advice letters in December 2005 to implement the $155 million pension-contribution revenue requirement for 2006 requested by PG&E in A.05-12-021. All three advice letters went into effect automatically on January 1, 2006. Although PG&E has been collecting the $155 million since January 1st, PG&E has not yet contributed any of the $155 million to its Pension trust.

On January 30, 2006, ALJs Kenney and Econome issued a ruling that required PG&E to file an advice letter to establish a memorandum account to accrue and track interest on the $155 million. In compliance with the ALJs' ruling, PG&E filed AL 2703-G/2782-E on February 10, 2006. The protest period for the AL passed without any protests or comments.

PG&E states that General Order (GO) 96-A provides that only ALs filed in compliance with Commission decisions may be approved by the Energy Division without a Commission resolution. Because AL 2703-G/2782-E was filed pursuant to an ALJ ruling, not a Commission decision, a Commission resolution is required to approve the AL unless other action is taken.

The Settling Parties request that today's Decision repeat the following language in the ALJs' ruling directing PG&E to file the AL:

> To ensure that the interest earned on the $155 million is used for its intended purpose, PG&E shall file an advice letter to establish a memorandum account to track the interest. The interest on the $155 million that is tracked by the memorandum account shall accrue from January 1, 2006, at the same short-term rate used by PG&E's Distribution Revenue Adjustment Mechanism and Utility Generation

> Balancing Account. The interest tracked by the memorandum account shall be contributed to PG&E's pension trust.

The Settling Parties state that including the above language in today's Decision (which we have just done) will allow the Energy Division (ED) to approve AL 2703-G/2782-E, or a slightly modified supplement to the AL, as being in compliance with a Commission decision. We find the Settling Parties' proposal to be reasonable. Therefore, ED may approve AL 2703-G/2782-E, or a slightly modified supplement to that AL, as being in compliance with today's Decision as long as ED finds that the AL implements the above language.

E. TURN's Proposal

We decline to adopt TURN's proposal to authorize PG&E to place up to 50% of its Pension trust's equity investments in the 36 utility companies that PG&E used in the most recent cost-of-capital proceeding to support PG&E's request for an ROE of 11.5%. TURN's proposal, if adopted, would cause a substantial reduction in the diversification of the PG&E's Pension trust portfolio. The reduced diversification would increase the risk of the portfolio, with risk defined as variability of returns. In general, pension plans should avoid such risk through diversification. Of course, higher risk is often associated with the potential for higher returns. However, TURN did not demonstrate that the projected risk-adjusted return for its proposal exceeds the projected risk-adjusted return for PG&E's current Pension trust portfolio.

The premise of TURN's proposal is that there should be a correlation between PG&E's authorized ROE, currently 11.35%, and the projected return on the Pension trust's equity investments, which is assumed by the Settlement to be approximately 8.5%. Even if TURN is correct, the fact that a correlation may exist does not support an inference that PG&E's authorized ROE is too high, the projected return on PG&E's Pension trust equity investments is too low, or some combination of the two. Nevertheless, TURN has raised a topic that is worth exploring. In future cost-of-capital proceedings, we will ask PG&E to explain and compare the equity markets data it used to prepare (1) its requested ROE, and (2) the pension costs reported in PG&E's most recent Form 10-K.

8. Categorization and Need for Hearing

In Resolution ALJ 176-3164, dated December 15, 2005, the Commission preliminarily categorized A.05-12-002 as a ratesetting proceeding and preliminarily determined that hearings were necessary. These preliminary determinations were affirmed by the Assigned Commissioner's Ruling and Scoping Memo dated February 3, 2006. There was no appeal of the Ruling.

In Resolution ALJ 176-3165, dated January 15, 2006, the Commission preliminarily categorized A.05-12-021 as a ratesetting proceeding and preliminarily determined that hearings were necessary. These preliminary determinations were affirmed by the Assigned Commissioner's Ruling and Scoping Memo dated February 1, 2006. There was no appeal of the Ruling.

9. Comments on the Proposed Decision

The proposed decision of the ALJ in this matter was mailed to the parties in accordance with Section 311(d) of the Public Utilities Code and Rule 77.1 of the Rules of Practice and Procedure. Comments regarding the proposed decision were filed on ___________, by ___________. Reply comments were filed on __________, by ___________.

10. Assignment of Proceeding

John A. Bohn is the Assigned Commissioner and Timothy Kenney is the assigned ALJ in this proceeding.

Findings of Fact

1. The funded status of PG&E's Pension Plan on January 1, 2005, was 98.6%. PG&E projects that the funded status will decline to 90.3% by January 1, 2009, if no pension contributions are made during 2006-08.

2. In A.05-12-002 and A.05-12-021, PG&E requests authority to (i) make contributions to its Pension Plan trust during 2006-09 to bring the funded status of the Plan to 100% by January 1, 2010, on a projected basis, and (ii) recover the GRC-related revenue requirement for the aforementioned pension contributions.

3. The attached Settlement Agreement allows PG&E to (i) make pension contributions during 2006-09 that will bring the funded status of the Pension Plan to 100% by January 1, 2010, on a projected basis, and (ii) recover the GRC-related revenue requirement for these pension contributions. The Settlement resolves all issues in A.05-12-021 and the pension issues in A.05-12-002.

4. The Settlement is supported by all parties that chose to participate actively in the settlement conference on February 24, 2006, and in the evidentiary hearing on March 20, 2006. There is no opposition to the Settlement.

5. The Settling Parties are fairly reflective of the affected interests.

6. The Settlement and the supporting record convey sufficient information to enable the Commission to discharge its regulatory obligations with respect to the parties and their interests.

7. Pursuant to D.05-12-046, PG&E's rates currently include $155 million to fund a pension contribution in 2006 of $249.7 million. The $155 million is subject to refund. PG&E has not yet made the contribution.

8. An ALJ ruling issued on January 23, 2006, directed PG&E to file an AL to establish a memorandum account to accrue and track interest on the $155 million that PG&E has been collecting in rates since January 1, 2006, pursuant to

D.05-12-046. The ruling also directed that the interest tracked by the memorandum account be contributed to PG&E's Pension trust. In compliance with the ALJ ruling, PG&E filed AL 2703-G/2782-E on February 10, 2006.

9. The Settlement makes permanent for 2006 (i.e., no longer subject to refund) the $155 million described in the previous Finding of Fact. The Settlement also requires PG&E to make no later than 40 days from the effective date of today's Decision a total pension contribution of $273.2 million for 2006, which equates to a net pension contribution (i.e., excluding Voluntary Retirement Incentives and PG&E Corporation) for 2006 of $249.7 million.

10. The Settlement requires PG&E to make a total pension contribution of $176.0 million annually during 2007-09, which equates to a net contribution of $153.4 million annually during 2007-09.

11. The Settlement provides for the establishment of a two-way balancing account for differences between authorized contributions to the Pension Plan trust and (i) lower contributions for any reason, or (ii) federally mandated higher contributions. Other balancing accounts would track differences between PG&E's authorized revenue requirement for pension contributions and the actual amount collected in rates.

12. The Settlement requires PG&E to file an annual report with the Commission, with service to DRA and CCUE, that states (i) the amount of pension contributions for the prior calendar year, (ii) the dates the contributions were made, and (iii) the calendar year-end value of Pension trust assets.

13. TURN proposes to allow PG&E to invest a significant portion of its Pension trust assets in the 36 utility companies that PG&E used to support its request for an ROE of 11.50% in PG&E's most recent cost-of-capital proceeding.

14. TURN's proposal would reduce the diversification of PG&E's portfolio of Pension trust assets, thereby increasing the risk of the portfolio. TURN did not demonstrate that the projected risk-adjusted return for its proposal would exceed the projected risk-adjusted return of PG&E's current portfolio.

15. The Settlement Agreement assumes that PG&E's Pension trust equity investments will earn an annual return of approximately 8.5%. By comparison, D.05-12-043 authorized an ROE for PG&E of 11.35% for 2006.

Conclusions of Law

1. No term of the Settlement Agreement attached to today's Decision contravenes statutory provisions or prior Commission decisions.

2. The Settlement is reasonable in light of the whole record, consistent with the law, and in the public interest.

3. The Settlement Agreement should be adopted.

4. PG&E should be authorized to make pension contributions in accordance with the Settlement Agreement and to recover the associated revenue requirement as set forth in today's Decision and the Settlement Agreement.

5. The adopted Settlement Agreement is binding on all parties to A.05-12-002 and A.05-12-021.

6. With one exception, the adoption of the Settlement Agreement does not constitute approval of, or precedent regarding, any principle or issue in this proceeding or in any future proceeding. The one exception is that the pension-related revenue requirement established in other proceedings should be consistent with the Settlement.

7. GO 96-A provides that only AL filings in compliance with Commission decisions may be approved by the Energy Division without a Commission resolution. AL 2703-G/2782-E was filed at the direction of an ALJ ruling, not a

Commission decision, so approval of the AL must be by a Commission resolution unless other action is taken.

8. The Energy Division should be authorized to approve PG&E's pending AL 2703-G/2782-E, or a slightly modified supplement to the AL, without a Commission resolution, if the AL does the following: (i) establishes a memorandum account to track interest earned on the $155 million that PG&E is currently collecting in rates; (ii) accrues interest beginning on January 1, 2006, at the same short-term rate used by PG&E's DRAM and UGBA; and (iii) requires that the tracked interest be contributed to PG&E's Pension trust.

9. TURN's proposal to allow PG&E to invest a significant portion of its Pension trust assets in 36 utility companies should not be adopted.

10. PG&E should identify, explain, and compare in future cost-of-capital proceedings the equity markets data and assumptions it used to prepare (i) PG&E's requested ROE, and (ii) the projected return on Pension trust equity investments reported in PG&E's most recent Form 10-K.

11. The following order should be effective immediately so that the Settlement Agreement may be implemented expeditiously.

O R D E R

IT IS ORDERED that:

1. The attached Settlement Agreement that was jointly filed by Pacific Gas and Electric Company (PG&E), the Division of Ratepayer Advocates (DRA), and the Coalition of California Utility Employees (CCUE) is adopted.

2. The $155 million that PG&E is currently collecting in rates pursuant to Decision 05-12-046 is no longer subject to refund.

3. The Energy Division may approve PG&E's pending Advice Letter (AL) 2703-G/2782-E, or a slightly modified supplement to the AL, without a Commission resolution, if the AL does all the following: (i) establishes a memorandum account to track interest earned on the $155 million described in the previous Ordering Paragraph; (ii) requires that accrual of interest begin on January 1, 2006, at the same short-term rate used by PG&E's Distribution Revenue Adjustment Mechanism and Utility Generation Balancing Account; and (iii) requires the tracked interest to be contributed to PG&E's Pension trust.

4. PG&E shall make contributions to its Pension Plan trust in 2006 through 2009 in accordance with the adopted Settlement Agreement.

5. PG&E is authorized to recover the revenue requirement for the portion of the pension contributions authorized herein that is allocable to PG&E's general rate case (GRC) lines of business. Recovery of the pension-contribution revenue requirement for non-GRC lines of business shall be authorized, as appropriate, in other proceedings and venues as set forth in the Settlement Agreement.

6. Within 60 days from the effective date of this Order, PG&E shall file an advice letter to establish a two-way balancing account for differences between authorized contributions to PG&E's Pension Plan trust and (i) lower contributions for any reason, or (ii) federally mandated higher contributions. The balancing account shall also comply with the requirements described in the body of today's Decision. So long as the advice letter conforms to today's Decision, the Commission's Energy Division may approve the advice letter without a Commission resolution.

7. PG&E shall file an annual report with the Commission, with service to DRA and CCUE, that states (i) the amount of pension contributions for the prior calendar year, (ii) the dates the contributions were made, and (iii) the calendar

year-end value of pension assets. PG&E shall file the report no later than February 15th of 2007 through 2010.

8. The Utility Reform Network's proposal to allow PG&E to invest a major portion of Pension trust assets in comparable utility companies is not adopted.

9. In future cost-of-capital proceedings, PG&E shall identify, explain, and compare the equity markets data and assumptions used to prepare (i) PG&E requested return on equity, and (ii) the projected return on PG&E's Pension trust equity investments reported in PG&E's most recent Form 10-K.

10. Application 05-12-021 is closed. Application 05-12-002 and Investigation 06-03-003 remain open to address all remaining GRC issues.

This order is effective today.

Dated____________, at San Francisco, California.

Appendix A

Settlement Agreement

Settlement in Applications 05-12-021 and 05-12-002

I. SETTLEMENT AGREEMENT

In accordance with Rule 51 et seq. of the Rules of Practice and Procedure of the California Public Utilities Commission (Commission or CPUC), the parties to this Settlement (Settling Parties) agree on a mutually acceptable outcome to all issues in Application (A.) 05-12-021, Application of Pacific Gas and Electric Company to Increase Gas and Electric Revenue Requirements, Rates, and Charges for a Pension Contribution, Effective January 1, 2006 (2006 Pension Contribution Application), and to the pension contribution issue in A.05-12-002, Application of Pacific Gas and Electric Company For Authority, Among Other Things, to Increase Rates and Charges for Electric and Gas Service Effective on January 1, 2007 (2007 General Rate Case, or GRC).

II. SETTLEMENT PARTIES

The Settling Parties are as follows: Coalition of California Utility Employees (CCUE); Division of Ratepayer Advocates (DRA); and Pacific Gas and Electric Company (PG&E)

III SETTLEMENT CONDITIONS

The Settling Parties agree this Settlement resolves the specified issues raised in A.05-12-021 and A.05-12-002 by the Settling Parties, subject to the following reservations:

1. This Settlement embodies the entire understanding and agreement of the Settling Parties with respect to the matters described, and it supersedes prior oral or written agreements, principles, negotiations, statements, representations, or understandings among the Settling Parties with respect to those matters.

2. This Settlement represents agreement among the Settling Parties to the facts and law as specified. Following Rule 51.8, the Settling Parties agree that this Settlement should not constitute precedent regarding any principle or issue in this proceeding or in any future proceeding.
3. The Settling Parties agree that this Settlement is reasonable in light of the testimony submitted, consistent with law, and in the public interest, in accordance with Rule 51.1(e).
4. The Settling Parties agree that no provision of this Settlement shall be construed against any Settling Party because that Settling Party or its counsel or advocate drafted the provision.
5. This Settlement may be amended or changed only by a written agreement signed by the Settling Parties.
6. The Settling Parties shall jointly request Commission approval of this Settlement and shall actively support prompt approval of the Settlement.
7. The Settling Parties intend the Settlement to be interpreted and treated as a unified, integrated agreement. In the event the Commission rejects or modifies this Settlement, the Settling Parties reserve their rights under Rule 51.7.

IV. SETTLEMENT HISTORY

In PG&E's 2003 test year GRC (A. 02-11-017 et al.), PG&E requested Commission approval of a net (i.e., excluding PG&E Corporation and Voluntary Retirement Incentive benefits) pension contribution amount of $128.6 million on a total company basis (including the gas transmission, electric transmission, and nuclear decommissioning lines of business), which translated into a total associated GRC revenue requirement of $74.8 million for PG&E's gas distribution, electric distribution, and electric generation lines of business. After litigation of this issue – the only revenue requirement issue in PG&E's 2003 GRC not addressed by the Distribution or Generation Settlements – the Commission denied PG&E's request in May 2004. (Decision (D.) 04-05-055, *mimeo*, pp. 5 and 77 and Findings of Fact 13-15 on pp. 129-30.)

In July 2005, PG&E filed the "Petition Of Pacific Gas And Electric Company To Modify Decision 04-05-055 Regarding Pension Contributions" (Petition), requesting an opportunity to show that it is prudent for the Commission to approve a resumption of pension contributions in 2006, and to approve recovery of that contribution in rates beginning January 1, 2006, subject to being credited back to ratepayers if the Commission later rules against PG&E on the merits.

On December 2, 2005 (prior to a Commission ruling on PG&E's Petition, and therefore assuming no net pension contribution in 2006), PG&E filed its 2007 test year GRC Application, requesting among other things that the Commission approve a net annual pension contribution amount of $343.9 million on a total company basis, which translates into a total associated GRC revenue requirement of $216.2 million.

On December 16, 2005, the Commission issued D.05-12-046 granting the Petition in part and denying it in part. Specifically, Ordering Paragraph 1 (pp. 11-12) of D.05-12-046 modified Finding of Fact 13 in D.04-05-055 to read as follows:

> The need for ratepayer contributions to the Retirement Plan trust should be based on the funding status of the Retirement Plan trust. PG&E may continue to evaluate the need for a contribution to the Retirement Plan trust. In the event PG&E determines that it would be prudent to resume contributions in 2006, PG&E is authorized to file an application for a revenue requirement increase to fund the estimated contribution for 2006 only, and PG&E is further authorized to make that revenue requirement effective in rates on January 1, 2006, subject to refund to PG&E ratepayers upon Commission determination of the merits of the application.

On December 20, 2005, PG&E filed A.05-12-021 requesting that the Commission approve a net pension contribution amount of $249.7 million on a total company basis for 2006, which translates into a total associated GRC revenue requirement of $155.0 million. At the same time, PG&E filed Advice 2686-G/2753-E to establish a mechanism to refund the revenue requirement increase to PG&E ratepayers to the extent the Commission determination of the merits of A.05-12-021 does not approve the requested amount in full. Later in December 2005, PG&E filed Advice 2678-G-A and Advice 2706-E-A to reflect the requested increase in gas and electric rates effective January 1, 2006.

On January 23, 2006, Administrative Law Judge (ALJ) Kenney, ALJ Econome, and Assigned Commissioner Bohn held a joint prehearing conference in A.05-12-002 and A.05-12-021. On February 10, 2006, following the ALJs' Ruling dated January 30, 2006, in A.05-12-021, PG&E filed Advice 2703-G/2782-E to establish gas and electric pension interest memorandum accounts for a 2006 contribution. On February 1, 2006, Commissioner Bohn issued his Assigned Commissioner's Ruling And Scoping Memo in A.05-12-021 (February 1 ACR), and on February 3, 2006, he issued his Assigned Commissioner's Ruling And Scoping Memo in A.05-12-002 (February 3 ACR). On February 10, 2006, Commissioner Bohn issued an Assigned Commissioner's Ruling Modifying Schedule in A.05-12-021.

The February 1 ACR (p. 3) addresses the possibility of a settlement as follows:

> The parties are encouraged to settle all issues. At a minimum, the parties should endeavor to reach a joint stipulation on material facts, such as (1) the current and projected funded status of PG&E's pension plan, (2) PG&E's pension contribution for calendar year 2006 assuming the Commission adopts PG&E's proposal to have PG&E's pension liability fully funded by January 1, 2010, and (3) the projected

> minimum contributions required by the Employee Retirement Income Security Act [ERISA] for each of the years 2006 through 2010.

On February 10, 2006, PG&E served Supplemental Pension Testimony (Exh. [PG&E-15]) in A.05-12-002, adjusting its 2007 GRC pension request in the event the Commission approves the 2006 Pension Contribution Application in full. The adjusted request for 2007 is a net pension contribution amount of $249.7 million on a total company basis, which translates into a total associated GRC revenue requirement of $157.8 million.

After providing notice to all parties pursuant to Rule 51.1(b) on February 15, 2006, PG&E hosted an initial settlement conference on February 24, 2006, on the 2006 Pension Contribution case and the pension contribution issue in the 2007 GRC. As a result of earlier discussions, PG&E and DRA announced to other parties at the conference that they had reached agreement in principle on the terms of a settlement. On February 28, 2006, counsel for DRA notified ALJ Kenney and the service lists for A.05-12-021 and A.05-12-002 of the agreement in principle. On March 3, 2006, CCUE agreed to support the settlement.

V. SETTLEMENT TERMS

The Settling Parties agree that since 1992 PG&E has not made any net pension contributions, and that on January 1, 2005, the funded status of PG&E's Retirement Plan trust was 98.6%. The Settling Parties further agree that this Settlement is intended to provide for pension contributions in the years 2006-09 that will result in PG&E's trust being fully funded on January 1, 2010, on a projected basis.

In order to reach agreement on the level of contributions PG&E should make in the years 2006-09 to reach fully funded status on January 1, 2010, on a projected basis, the Settling Parties agree to adjust PG&E's pension proposal in the 2006 Pension Contribution Application and 2007 GRC Application in the following three ways: first, take into account the actual 2005 year-end return on assets (information that was not available when PG&E filed A.05-12-021); second, make final (i.e., not subject to refund) the amount of $155.0 million being collected in rates in 2006, so PG&E will make a net pension contribution of $249.7 million for 2006; and third, change the assumed annual return on Retirement Plan trust assets for 2006-09 from 7.0% to 7.5%. With these three adjustments, the Settling Parties agree that the total and net pension contributions required to reach fully funded status on January 1, 2010, on a projected basis, are $273.2 million and $249.7 million in 2006, and $176.0 million and $153.4 million in 2007-09. The following paragraphs explain these three adjustments in more detail.

According to the 2006 Pension Contribution Application and 2007 GRC Application (as supplemented by testimony served February 10, 2006), PG&E estimated the net pension contribution and associated GRC revenue requirement necessary to reach fully funded status on January 1, 2010, on a projected basis, are $249.7 million and $155.0 million in 2006 (Exh. (PG&E-1), p. ES-1 in A.05-12-021), and $249.7 million and $157.8 million for each of the three years 2007-09 (Exh. (PG&E-15), pp. 2-1 and 3-1 in A.05-12-002). PG&E's analysis is that, beginning with the funded status of 98.6% as of January 1, 2005, and assuming a level annual net pension contribution for the four years 2006-09 and an annual return on assets of 7.0% for the five years 2005-09, PG&E's proposed funding level would result in a funding status of 100.0% on January 1, 2010, on a projected basis. Under the assumption of an annual return on assets of 7.0% for the five years 2005-09, absent any net pension contributions before 2010, the funded status of PG&E's Retirement Plan trust on the first of the year and the minimum contribution required by ERISA each year is projected to be as follows: for 2006, 96.8% and zero; for 2007, 94.8% and zero; for 2008, 92.6% and zero; for 2009, 90.3% and $308.0 million; and for 2010, 90.9% and $735 million. (Exh. [PG&E-1], pp. 1-6, 1-A9, and 2-4.)

Pursuant to this Settlement, the first adjustment to PG&E's proposal is to take into account the actual 2005 year-end return on assets, information that was not available when PG&E filed A.05-12-021. At year-end 2005, PG&E's Retirement Plan trust assets had earned a return that exceeded the expected return of 7.0%. Updating the Plan's funded status for the actual Plan return in 2005, the contributions in 2006-09 needed to reach fully funded status on January 1, 2006, on a projected basis, are lower than PG&E had calculated in its proposal. (Declaration of Peter Corippo, attached.)

The second adjustment is to make final (i.e., not subject to refund) the amount of $155.0 million being collected in rates in 2006, so PG&E will make a total pension contribution of $273.2 million for 2006 which equates to $249.7 million on a net basis. This contribution lowers the contributions in 2007-09 needed to reach fully funded status on January 1, 2010, on a projected basis. (Declaration of Peter Corippo.)

The third adjustment is to change the assumed annual return on Retirement Plan trust assets for 2006-09 from 7.0% to 7.5%. Given the relatively short four-year time frame, in which volatility can be expected, an assumption of a trust return of 7.5% for the purposes of this Settlement is reasonable. If actual trust performance in 2006-2009 meets the assumed 7.5% return, then the funded status is projected to be 100.0% on January 1, 2010. (Declaration of Peter Corippo.)

As set forth in this Settlement, it is prudent for PG&E to resume pension contributions beginning in 2006 and continuing through 2009. (Declaration of Deborah Dubois, attached.)

Given these three adjustments, the annual net pension contribution and associated revenue requirement in 2006 are $249.7 million and $155.0 million, respectively, as PG&E proposed, while the annual amounts for 2007-09 are $153.4 million and (estimated at) $98.2 million, respectively. (Declaration of Peter Corippo; Declaration of Pamela Nordin, attached.) Thus the revenue requirements under this Settlement remain the same as in PG&E's proposal for 2006 ($155.0 million), while they are estimated to be reduced by $59.6 million compared to PG&E's proposal for 2007-09 ($157.8 million to $98.2 million.) As a result, for 2007-09 the pension-related revenue requirement will be approximately $56.8 million lower than in 2006 ($155.0 million to $98.2 million.) For 2006, the pension-related revenue requirement of $155.0 million consists of $43.3 million for gas distribution, $77.2 million for electric distribution, and $34.5 million for electric generation. (Exh. (PG&E-1), pp. ES-1 to ES-2 in A.05-12-021.) For 2007-09, the estimated pension-related revenue requirement of $98.2 million consists of $26.2 million for gas distribution, $46.7 million for electric distribution, and $25.3 million for electric generation. (Declaration of Pamela Nordin.)

In addition to agreement on the net pension contribution and pension-related revenue requirement amounts for 2006-09, the Settling Parties agree to the following additional conditions as part of this Settlement:

1. The Settling Parties agree that the Commission should establish a two-way balancing account for differences between authorized contributions to the trust and 1) lower contributions for any reason or 2) federally mandated higher contributions.

2. The Settling Parties agree that, if this Settlement is adopted by the Commission, the following testimony should be admitted into evidence without cross-examination by the Settling Parties: in A.05-12-021, Exh. (PG&E-1); in A.05-12-002, Exh. (PG&E-6), p. 18-2 line 9 through p. 18-15 line 15 of Chapter 18, Appendix A to Chapter 18, and Chapter 19; in A.05-12-021 and A.05-12-002, this Settlement and the attached Declarations of Peter Corippo, Deborah Dubois, and Pamela Nordin. If this Settlement is not adopted, the Settling Parties reserve their cross-examination rights.

3. The Settling Parties agree that the chart on page 11 of this Settlement constitutes the comparison exhibit showing the impact of the Settlement in relation to the litigation positions of PG&E, as required by Rule 51.1(c). The Settling Parties further agree that since DRA has not submitted testimony establishing a litigation position, Rule 51.1(c) does not require a comparison exhibit for DRA.

4. The Settling Parties agree that non-GRC rate impacts (i.e., pension-related revenue requirements for gas transmission, electric transmission, and nuclear decommissioning) are being addressed in other proceedings. For gas transmission, PG&E will not request any change in the Gas Accord III Settlement Agreement approved in D.04-12-050. For electric transmission, the relevant proceeding is PG&E's eighth Transmission Owner Tariff rate filing at the Federal Energy Regulatory Commission, Docket No. ER 05-1284-000. For nuclear decommissioning, the relevant proceeding is the Nuclear Decommissioning Triennial Cost Proceeding, A.05-11-009.

5. Within 40 days after the Commission issues a final decision approving this Settlement, PG&E agrees to make a total company pension contribution of $273.2 million in 2006 which equates to a net pension contribution (excluding VRI and Corporation) of $249.7 million.

6. Unless superseded by additional condition 1, above, after the Commission issues a final decision approving this Settlement, PG&E agrees to make total company pension contributions of $176.0 million for each of the years 2007, 2008 and 2009, which equates to a net contribution of $153.4 million. PG&E will make quarterly contributions to its pension fund during these years consistent with its Working Cash study. These quarterly payment dates are April 15, July 15, October 15 and January 15 for each annual payment cycle.

7. PG&E will file an annual report with the Commission, with service to DRA and CCUE, verifying the amount of pension contributions and dates that the contributions were made. The report shall also include the actual pension asset valuation at year end.

8. The Settling Parties agree that Commission approval of this Settlement will impose no restrictions on PG&E's pension contribution request in its 2010 GRC Application or on positions taken by any other party in that proceeding.

The major terms of this Settlement as described above are shown on page 11.

Annual Pension Contributions and Related Revenue Requirements

(in millions)

	As requested by PG&E	As agreed to by Settling Parties
Total Contribution (2006 / annually 2007-09)	$273.2 / $273.2	$ 273.2 / $176.0
Net Contribution, excl. VRI and Corp. (2006 / annually 2007-09)	$249.7 / $249.7	$249.7 / $153.4
Total Company Revenue Requirement (2006 / annually 2007-09)	$176.5 / $178.8	$ 176.5 / $111.3*
GRC Lines of Business (2006 / annually 2007-09)	$155.0 / $157.8	$ 155.0 / $98.2*
* These are currently estimated figures based on PG&E's 2007 GRC filing, and proposed assumptions and allocation factors. If the final adopted figures are different from PG&E's assumptions, that may impact the revenue requirement associated with this pension contribution.		

Settlement Elements

- Settle for all 4 years, 2006 through 2009 in both proceedings.
- Update for year-end 2005 asset values.
- Assume 7.0% discount rate for liabilities, as proposed by PG&E.
- Assume 7.5% return on pension assets, compared to PG&E's proposed 7.0%.
- Establish a two-way balancing account for differences between authorized contributions to the trust and 1) lower contributions for any reason or 2) federally mandated higher contributions.
- No restrictions on PG&E pension request in 2010 GRC or on positions taken by any other party in that proceeding.

Settlement Rate Impacts

- In 2006, no additional GRC rate impact (i.e., $155.0 million stays in rates through 12/31/06, not subject to refund).
- In 2007-09, GRC rates are estimated to be $56.8 million lower than in 2006.
- Non-GRC rate impacts (gas transmission, electric transmission, and nuclear decommissioning) to be addressed in other proceedings.

VI. SETTLEMENT EXECUTION

This document may be executed in counterparts, each of which shall be deemed an original, but all of which together shall constitute one and the same instrument. This Settlement shall become effective among the Settling Parties on the date the last Settling Party executes the Settlement as indicated below. In witness whereof, intending to be legally bound, the Settling Parties hereto have duly executed this Settlement on behalf of the Settling Parties they represent.

This Settlement is executed in counterparts, each of which shall be deemed an original. The undersigned represent that they are authorized to sign on behalf of the Party represented.

Coalition of California Utility Employees

Signature: /s/
Name: Tanya A. Gulesserian
Title: Attorney
Date: March 8, 2006

Division of Ratepayer Advocates

Signature: /s/
Name: R. Mark Pocta
Title: Program Manager
Date: March 8, 2006

Pacific Gas and Electric Company

Signature: /s/
Name: Andrew L. Niven
Title: Attorney
Date: March 8, 2006

DECLARATION OF PETER CORIPPO

I, Peter Corippo, declare:

1. I am employed by PG&E Corporation as the Director of Investments and Benefit Finance. In that capacity, I am responsible for making recommendations concerning the funding and investment management for the employee benefit plans sponsored by Pacific Gas and Electric Company (PG&E), including the PG&E Retirement Plan (Plan). I make this Declaration in support of the Settlement of PG&E, Division of Ratepayer Advocates, and Coalition of California Utility Employees regarding pension contributions for 2006-09 in Applications 05-12-021 and 05-12-002.

2. The purpose of this Declaration is to state the impact of the Settlement on the Plan's projected funded status. Exhibit (PG&E-15) in Application 05-12-002 indicates that net pension contributions of $249.7 million ($273.2 million on a total basis, including PG&E Corporation and Voluntary Retirement Incentive benefits) annually in 2006-2009 would result in a projected funded status of 100 percent on January 1, 2010. The Settlement preserves the $249.7 million amount in 2006 but reflects lower net pension contributions of $153.4 million ($176.0 million on a total basis) in 2007-2009. These lower contributions result from (1) an update for actual Plan investment returns in 2005 that exceeded the expected return of 7.0 percent and (2) an increase in assumed Plan returns from 7.0 percent to 7.5 percent in 2006-2009. Given the relatively short four-year time frame, in which volatility can be expected, an assumption of trust returns in the range of 7.0 percent to 7.5 percent for the purposes of this Settlement is reasonable. Changing the return to 7.5 percent brings PG&E's projected trust return for this period in line with those of Southern California Edison Company and San Diego Gas & Electric Company, which are also at 7.5 percent, notwithstanding PG&E's testimony as to demographic and investment profile differences between PG&E and the other companies. If actual trust performance in 2006-2009 is 7.5 percent, the Plan's funded status is projected to be 100.0 percent on January 1, 2010.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct. Executed this 7th day of March, 2006, at San Francisco, California.

/s/

PETER CORIPPO

DECLARATION OF DEBORAH DUBOIS

I, Deborah Dubois, declare:

1. I am a recently-retired Principal of Towers Perrin but continue to work part time on a contract basis for a small number of clients, including Pacific Gas and Electric Company (PG&E). Towers Perrin is a global professional services firm providing a wide range of human resource and financial services industry consulting. Prior to my official retirement, I was consultant to several major clients on actuarial and benefits issues, including retirement plan design and funding strategy. I have been a Fellow of the Society of Actuaries since 1984. I make this Declaration in support of the Settlement of PG&E, Division of Ratepayer Advocates, and Coalition of California Utility Employees regarding pension contributions for 2006-09 in Applications 05-12-021 and 05-12-002.
2. The purpose of this Declaration is to certify that the forecasts presented in the Declaration of Peter Corippo were prepared by me or under my direction and are actuarially sound, and to state my professional opinion based on the results of these forecasts.
3. Based on the results of the forecasts in the Declaration of Peter Corippo, my professional opinion is that it is prudent for Pacific Gas and Electric Company to resume regular pension contributions beginning in 2006 with the objective of restoring the Pacific Gas and Electric Company Retirement Plan's projected funded status to 100 percent by the beginning of 2010 assuming the trust earns 7.5 percent annually in 2006-2009.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed this 7th day of March, 2006, at San Francisco, California.

/s/

DEBORAH DUBOIS

DECLARATION OF PAMELA NORDIN

I, Pamela Nordin, declare:

1. I am employed by Pacific Gas and Electric Company (PG&E) as a team lead in the Administrative and General (A&G) Expense Recovery section of PG&E's Operations Revenue Requirements Department. This section is responsible for A&G expense forecasts, studies, and analyses. I make this declaration in support of the Settlement of PG&E, Division of Ratepayer Advocates, and Coalition of California Utility Employees regarding pension contributions for 2006-09 in Applications 05-12-021 and 05-12-002.

2. The purpose of this Declaration is to record the impact of the Settlement on the revenue requirement associated with a net pension contribution of $153.4 million in 2007-2009. For 2007-2009, the pension-related revenue requirement is $98.2 million, consisting of $26.2 million for gas distribution, $46.7 million for electric distribution, and $25.3 million for electric generation, as demonstrated in Tables 1 to 6, attached. The revenue requirement was calculated using the cost pool allocation factors and unbundling method and Operations and Maintenance (O&M) labor factors proposed by PG&E in its 2007 General Rate Case Application (A.05-12-002). If the Commission adopts factors other than those proposed by PG&E, the pension-related revenue requirement would change.

I declare under penalty of perjury under the laws of the State of California that the foregoing is true and correct.

Executed this 7th day of March, 2006, at San Francisco, California.

/s/

PAMELA NORDIN

TABLE 1
Pacific Gas and Electric Company
Pension Revenue Requirement
Summary Calculation
(Millions of Dollars)

Line No.	Description	2007 Pension Contribution Revenue Requirement	Line No.
1	Pension Revenue Requirement Included In The 2007 GRC Application <1>	216.2	1
2	Reduction Resulting From Decreased Pension Contribution <2>	(118.0)	2
3	Revised Pension Revenue Requirement <3>	98.2	3

Notes:
<1> A.05-12-021, page 4.
<2> See attached Table 3, line 3.

<3> This revenue requirement is for GRC lines of business only. The total company revenue requirement is $111.3 million. See attached Table 2. These tables provide the results of running the Results of Operations model with a pension contribution of $1

TABLE 2
Pacific Gas and Electric Company
Pension Revenue Requirement
Unbundled Cost Category Summary
(Millions of Dollars)

Line No.			2007	Line No.
	Unbundled Cost Category Allocations <1>:			
1	Electric Distribution	42.02%	46.7	1
2	Gas Distribution	23.53%	26.2	2
3	Electric Generation	22.70%	25.3	3
4	GRC Subtotal	88.25%	98.2	4
5	Nuclear Decom	0.51%	0.6	5
6	Electric Trans	6.51%	7.2	6
7	Gas Trans	4.73%	5.3	7
8	Subtotal	11.75%	13.1	8
9	Total Company	100.00%	111.3	9

Note:

<1> Per 2007 GRC Application (A.05-12-002). See page 6-15 of the workpapers supporting chapter 6 of Exhibit (PG&E-2).

TABLE 3
Pacific Gas and Electric Company
2007 General Rate Case Application - Jan Update-Escalated vs. Jan Update w/'06-07 Pension Contribution
Results of Operations - Test Year 2007
Total Electric Distribution, Gas Distribution, and Electric Generation
(Thousands of Dollars)

Line No.	Description	PG&E Jan. Update	PG&E Jan. Update w/'06-07 Pension	Difference: Jan. Update Greater than PG&E Jan. Update w/'06-07 Pension	Line No.
	REVENUE				
1	Revenue at Effective Rates	5,285,168	5,167,216	117,953	1
2	Less Non-General Revenue	91,287	91,287	0	2
3	General Rate Case Revenue	5,376,455	5,258,503	117,953	3
	OPERATING EXPENSES				
4	*Energy Costs	0	0	0	4
5	*Other Production	451,771	451,771	0	5
6	*Storage	0	0	0	6
7	*Transmission	10,118	10,118	0	7
8	*Distribution	643,315	643,315	0	8
9	*Customer Accounts	433,691	433,691	0	9
10	Uncollectibles	15,583	15,242	341	10
11	*Customer Services	15,579	15,579	0	11
12	*Administrative and General	865,628	752,642	112,986	12
13	Franchise Requirements	42,832	41,879	953	13
14	Amortization	6,476	6,476	0	14
15	Wage Change Impacts	0	0	0	15
16	Other Price Change Impacts	0	0	0	16
17	*Other Adjustments	(11,657)	(11,657)	0	17
18	Subtotal Expenses	2,473,337	2,359,056	114,280	18
	TAXES				
19	Superfund	0	0	0	19
20	Property	138,013	138,013	0	20
21	Payroll	82,124	82,124	0	21
22	Business	832	832	0	22
23	Other	233	233	0	23
24	State Corporation Franchise	113,831	113,971	(140)	24
25	Federal Income	445,703	445,135	569	25
26	Total Taxes	780,736	780,307	429	26
27	Depreciation	1,024,481	1,023,100	1,381	27
28	Fossil Decommissioning	(30,046)	(30,046)	0	28
29	Nuclear Decommissioning	0	0	0	29
30	Total Operating Expenses	994,435	993,054	1,381	30
31	Net for Return	1,127,948	1,126,086	1,862	31
32	Rate Base	12,834,220	12,813,029	21,191	32
	RATE OF RETURN				
33	On Rate Base	8.79%	8.79%	0.00%	33
34	On Equity	11.35%	11.35%	0.00%	34

TABLE 4
Pacific Gas and Electric Company
2007 General Rate Case Application - Jan Update-Escalated vs. Jan Update w/'06-07 Pension Contribution
Results of Operations - Test Year 2007
Electric Distribution
(Thousands of Dollars)

Line No.	Description	PG&E JanUpdate	PG&E JanUpdate w/'06-07 Pension	Difference: PG&E Jan. Update Greater than PG&E Jan. Update w/'06-07 Pension	Line No.
	REVENUE				
1	Revenue at Effective Rates	3,060,461	3,004,320	56,140	1
2	Less Non-General Revenue	90,027	90,027	0	2
3	General Rate Case Revenue	3,150,488	3,094,347	56,140	3
	OPERATING EXPENSES				
4	*Energy Costs	0	0	0	4
5	*Other Production	0	0	0	5
6	*Storage	0	0	0	6
7	*Transmission	726	726	0	7
8	*Distribution	504,675	504,675	0	8
9	*Customer Accounts	253,577	253,577	0	9
10	Uncollectibles	9,173	9,010	163	10
11	*Customer Services	3,373	3,373	0	11
12	*Administrative and General	412,188	358,387	53,801	12
13	Franchise Requirements	23,840	23,416	425	13
14	Amortization	0	0	0	14
15	Wage Change Impacts	0	0	0	15
16	Other Price Change Impacts	0	0	0	16
17	*Other Adjustments	(9,197)	(9,197)	0	17
18	Subtotal Expenses	1,198,355	1,143,966	54,389	18
	TAXES				
19	Superfund	0	0	0	19
20	Property	91,280	91,280	0	20
21	Payroll	38,480	38,480	0	21
22	Business	390	390	0	22
23	Other	109	109	0	23
24	State Corporation Franchise	79,158	79,224	(66)	24
25	Federal Income	311,474	311,202	272	25
26	Total Taxes	520,890	520,685	205	26
27	Depreciation	679,393	678,736	658	27
28	Fossil Decommissioning	0	0	0	28
29	Nuclear Decommissioning	0	0	0	29
30	Total Operating Expenses	2,398,638	2,343,386	55,252	30
31	Net for Return	751,849	750,961	888	31
32	Rate Base	8,554,825	8,544,719	10,107	32
	RATE OF RETURN				
33	On Rate Base	8.79%	8.79%	0.00%	33
34	On Equity	11.35%	11.35%	0.00%	34

TABLE 5
Pacific Gas and Gas Company
2007 General Rate Case Application - Jan Update-Escalated vs. Jan Update w/'06-07 Pension Contribution
Results of Operations - Test Year 2007
Gas Distribution
(Thousands of Dollars)

Line No.	Description	PG&E Jan. Update	PG&E Jan. Update w/'06-07 Pension	Difference: Jan. Update Greater than PG&E Jan. Update w/'06-07 Pension	Line No.
	REVENUE				
1	Revenue at Effective Rates	1,124,156	1,092,665	31,491	1
2	Less Non-General Revenue	0	0	0	2
3	General Rate Case Revenue	1,124,156	1,092,665	31,491	3
	OPERATING EXPENSES				
4	*Energy Costs	0	0	0	4
5	*Other Production	0	0	0	5
6	*Storage	0	0	0	6
7	*Transmission	3,789	3,789	0	7
8	*Distribution	138,640	138,640	0	8
9	*Customer Accounts	180,114	180,114	0	9
10	Uncollectibles	3,201	3,112	90	10
11	*Customer Services	12,206	12,206	0	11
12	*Administrative and General	230,811	200,684	30,127	12
13	Franchise Requirements	10,654	10,355	298	13
14	Amortization	0	0	0	14
15	Wage Change Impacts	0	0	0	15
16	Other Price Change Impacts	0	0	0	16
17	*Other Adjustments	(2,460)	(2,460)	0	17
18	Subtotal Expenses	576,956	546,441	30,515	18
	TAXES				
19	Superfund	0	0	0	19
20	Property	22,912	22,912	0	20
21	Payroll	21,933	21,933	0	21
22	Business	222	222	0	22
23	Other	62	62	0	23
24	State Corporation Franchise	20,122	20,160	(38)	24
25	Federal Income	78,817	78,666	151	25
26	Total Taxes	144,068	143,955	113	26
27	Depreciation	209,788	209,420	368	27
28	Fossil Decommissioning	0	0	0	28
29	Nuclear Decommissioning	0	0	0	29
30	Total Operating Expenses	930,812	899,816	30,996	30
31	Net for Return	193,344	192,849	494	31
32	Rate Base	2,199,940	2,194,314	5,626	32
	RATE OF RETURN				
33	On Rate Base	8.79%	8.79%	0.00%	33
34	On Equity	11.35%	11.35%	0.00%	34

TABLE 6
Pacific Gas and Electric Company
2007 General Rate Case Application - Jan Update-Escalated vs. Jan Update w/'06-07 Pension Contribution
Results of Operations - Test Year 2007
Electric Generation
(Thousands of Dollars)

Line No.	Description	PG&E Jan. Update	PG&E Jan. Update w/'06-07 Pension	Difference: Jan. Update Greater than PG&E Jan. Update w/'06-07 Pension	Line No.
	REVENUE				
1	Revenue at Effective Rates	1,100,552	1,070,230	30,322	1
2	Less Non-General Revenue	1,260	1,260	0	2
3	General Rate Case Revenue	1,101,812	1,071,490	30,322	3
	OPERATING EXPENSES				
4	*Energy Costs	0	0	0	4
5	*Other Production	451,771	451,771	0	5
6	*Storage	0	0	0	6
7	*Transmission	5,603	5,603	0	7
8	*Distribution	0	0	0	8
9	*Customer Accounts	0	0	0	9
10	Uncollectibles	3,208	3,120	88	10
11	*Customer Services	0	0	0	11
12	*Administrative and General	222,630	193,571	29,059	12
13	Franchise Requirements	8,338	8,108	229	13
14	Amortization	6,476	6,476	0	14
15	Wage Change Impacts	0	0	0	15
16	Other Price Change Impacts	0	0	0	16
17	*Other Adjustments	0	0	0	17
18	Subtotal Expenses	698,026	668,649	29,377	18
	TAXES				
19	Superfund	0	0	0	19
20	Property	23,821	23,821	0	20
21	Payroll	21,711	21,711	0	21
22	Business	220	220	0	22
23	Other	61	61	0	23
24	State Corporation Franchise	14,552	14,588	(36)	24
25	Federal Income	55,413	55,267	146	25
26	Total Taxes	115,778	115,667	110	26
27	Depreciation	135,300	134,944	355	27
28	Fossil Decommissioning	(30,046)	(30,046)	0	28
29	Nuclear Decommissioning	0	0	0	29
30	Total Operating Expenses	919,057	889,215	29,842	30
31	Net for Return	182,755	182,275	480	31
32	Rate Base	2,079,456	2,073,997	5,459	32
	RATE OF RETURN				
33	On Rate Base	8.79%	8.79%	0.00%	33
34	On Equity	11.35%	11.35%	0.00%	34